MEDPAC Medicare Payment Advisory Commission

MEETING BRIEF

December 13-14, 2001

Assessing payment adequacy and updating payments in the home health prospective payment system

ISSUE: Are current payments adequate? How much will efficient providers' costs grow over the next year? The answers to these two questions will form the basis of our update recommendation for home health as well as our response to two imminent payment changes—the implementation of the so-called 15 percent cut and the sunset of the 10 percent rural add-on.

KEY POINTS: We do not have an estimate of the current level of costs and payments. Market conditions suggest that access to care is good, the volume of episodes is stable, and exit and entry of providers is stable. We have no evidence that payments are inadequate or over adequate.

We expect providers' costs to grow over the next year and so payments must change to maintain the appropriate relationship of payments to costs. Our default measure of cost growth is the forecast change in the market basket. However, providers' costs might grow somewhat more slowly than the market basket because of declining visit-per-episode volume, and therefore you could concur with the update factor in current law of market basket minus 1.1.

An additional reduction of the base rate—the 15 percent cut—is scheduled for October 2002. Since the intended outcomes of the legislation of which the cut is the last phase have largely been achieved by the already-implemented phases, the cut may no longer be appropriate.

In June of this year, we concluded that the PPS should work as well in rural areas as in urban but acknowledged that low visit volume and distance to travel might cause rural costs to differ from urban costs. We still cannot measure the costs of rural home health; but the sharp decline in volume immediately preceding the implementation of the PPS and the greater exit of agencies in rural areas lead us to err on the side of one more year of additional payments (instead of reducing rural payments by 10 percent) until further data are available.

ACTION: Staff asks the Commissioners to consider recommendations on the adequacy of the base rate, the update factor, the 15 percent cut, and the rural add on.

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MEETING BRIEF

December 13-14, 2001

Payment adequacy and update: skilled nursing facility care

ISSUE: Is the current base payment rate (pool of money available) adequate for skilled nursing facility (SNF) care? Are payments distributed appropriately? If not, what should be done about it? At what rate should SNF payments be updated in 2003?

KEY POINTS: To determine whether Medicare payments are appropriate, we examine whether costs are appropriate and consider the relationship of payments to costs and other indicators of adequacy of payments.

- For freestanding SNFs, costs per day have dropped under PPS. SNFs have been able to renegotiate contracts, substitute low- for high-cost staff, and cut therapy staff. Hospital-based SNFs' costs, however, are difficult to interpret because hospitals historically have allocated costs to their SNFs.
- We also consider market conditions that may suggest whether payments are inadequate and the relationship between Medicare payments and costs.
    - According to the Office of Inspector General, beneficiaries are not experiencing widespread problems accessing SNF care.
    - Almost 20 percent of hospital-based SNFs have exited the Medicare program since the PPS was instituted, compared to a 1 percent increase in freestanding SNFs. Particularly notable is a 32 percent decrease in Medicare-only hospital-based SNFs.
    - The 1999 overall margin for SNFs was –5 percent. The Medicare margin for freestanding SNFs rose consistently under the PPS—from 0.3 percent during the first year of PPS in 1998 to 9.0 percent in 1999. During the same period, the Medicare margin for hospital-based SNFs dropped from –25.9 percent in 1998 to –55.6 percent in 1999.
    - Staff will present estimated Medicare margins for FY 2002, with policy changes that will take effect in 2003. Even without these results, however, we know that margins will be higher in 2003 than in 1999 because one temporary rate increase from BBRA (revised by BIPA) will still be in effect.

The distribution of payments appears to be inappropriate. The FY 1999 margins suggest that payments are more than adequate for freestanding SNFs and less than adequate for hospital-based SNFs. The negative margin for hospital-based SNFs is greater than we would expect as a function of cost misallocation and a significant number of these SNFs have exited the program. Fixing the classification system to address inappropriate distribution is not an option until 2006 at the earliest. Therefore, Commissioners may consider different payment updates for freestanding and hospital-based SNFs. Current law requires that SNF payments be updated by market basket –0.5 percent.

ACTION: Commissioners should make decisions about:

- Whether the SNF base payment rate is adequate.
- Whether the distribution of payments is appropriate and, if not what should be done about it.
- The rate at which SNF payments should be updated in 2003.

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